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SUBJECT: BACKGROUND AND TALKING
POINTS ON U.S. POSITION REGARDING
NORDSTREAM PIPELINE

REF: STOCKHOLM 611

¶1. (SBU) The United States supports reducing Russia's dominance in European gas markets through development of a Southern Corridor bringing gas from the Caspian region through Turkey to European markets. Nordstream bolsters Gazprom's position in European gas markets and could negatively impact the energy security of Ukraine, the Baltic littoral states and Poland. However, Nordstream's energy security implications for Europe require a nuanced approach. The United States should not advocate a view opposing the development of Nordstream. If asked for United States' views, Posts may draw from points provided below.

Background

¶2. (SBU) As planned, the European Commission (EC) supports Nordstream because it is a project to bring additional Russian gas to Europe to meet its growing demand, rather than diverting gas that currently transits Poland and Ukraine. Nordstream is planned to consist of two parallel pipelines each designed to deliver 27.5 billion cubic meters per year (bcm/a); the first pipeline is scheduled to be completed in 2011 and the second in 2012, for a total capacity of 55 bcm/a mainlined from Russia to Germany. The primary source of gas for the first pipeline, the Russian Yuzhno-Russkoye field (25 percent owned by German firm BASF), is projected to reach its planned output of 25 bcm/a in 2009, two-years ahead of schedule. However, other Russian sources of supply for Nordstream's second pipeline, the Bovanenko field on the Yamal Peninsula and the Shtokman field in the Barents Sea, are several years behind schedule and may not be ready in time for the second phase.

¶3. (SBU) In the event of production delays, it is unclear where gas to fill the second phase of Nordstream would come from. If the second phase of Nordstream diverts current volumes of gas transiting other nations through existing or inexpensively-upgraded infrastructure, then it could possibly harm the energy security of some eastern EU members and Ukraine. We should highlight this possibility to European nations that favor Nordstream. We indeed seek to explore with Kyiv and our EU partners the possibility of expanding gas transit across Ukraine by 20 bcm/a, a project Ukrainian authorities estimate would cost around USD 800 million.

¶4. (SBU) USG policy is to encourage Russia to increase

its oil and gas production to boost supply on global markets. USG attempts to oppose or undermine projects that bring additional gas to market could contradict our 2006 G-8 St. Petersburg Energy Security Principles commitments.

¶ 15. (SBU) We also strongly support the efforts of the European Commission to create a common EU internal market for gas and electricity along the lines envisioned in the Third Energy Package. A unified energy market, with increased electricity and gas interconnections between EU members, would significantly enhance European energy security. Currently Russia faces 27 separate European markets. If it faced one unified market the dynamics of the relationship could change positively. Greater interconnectivity also would help mitigate the risk from asymmetric shocks to one EU member.

¶ 16. (SBU) Both Germany and the Netherlands have supported Nordstream, ostensibly to compensate for declining North Sea production. At the same time, Chancellor Merkel inherited Nordstream from former Chancellor Schroeder, who concluded the deal shortly before assuming a position at the head of the Nordstream development company, Nordstream AG, a joint venture between Gazprom and German energy companies. Following Russia's attack on Georgia, Germany

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may be more sensitive to the possible downsides of Nordstream and the corresponding value of diversification options. Nordstream causes concern among other EU members, such as the Baltic States.

¶ 17. (SBU) Department requests Posts draw from the following talking points regarding the U.S. position on Nordstream if raised:

BEGIN POINTS

-- The EU and United States oppose business as usual with Moscow, as long as Russia is in violation of its commitments
Under ceasefire documents signed by President Medvedev.

-- It is important for Europe and the United States to work together to increase diversification of energy supplies. The key to this objective in Europe is the realization of a "Fourth" or "Southern Corridor" to export Caspian gas directly to Europe.

-- U.S. policy is to support EU efforts to diversify sources of energy supply, as well as to develop transparent, market oriented pipelines, which meet the best international practices for governance, transparency and environmental safety. This is consistent with the 2006 St. Petersburg Global Energy Security Principles that all G-8 members pledged to uphold.

-- Our central - and long held - position is that diversification of energy supplies will benefit both consumers and suppliers and improve European energy security.

-- Another core goal is full integration of European energy markets into a single market space. A common EU internal market for gas and electricity, as envisioned in the Third Energy Package proposed by the European Commission, would increase electricity and gas interconnections between Member States, boosting efficiency and enhancing EU energy security.

-- These internal reforms and diversification of energy sources are increasingly important given growing doubts as to whether Russia can produce enough gas to meet growing European demand. We encourage Western investment in new Caspian gas reserves so that these additional volumes can flow to the European market via new, non-Gazprom infrastructure.

The IEA has said that Russia could encounter problems fulfilling its existing European gas contracts as early as 2011 absent significant upstream investment; Russian gas production declined in 2007 for the first time since 2000, according to the 2008 BP Statistical Review of World Energy.

-- While Gazprom has said it will boost upstream gas investment, and Russia has announced domestic gas price increases to reduce demand, it is unclear whether such measures will have a concrete impact on increasing gas available for export.

-- If competition deepens more generally in the European gas and electricity markets, including by building interconnections among European natural gas and electricity grids (especially those that connect Germany to Poland and the Baltic states), Nordstream's potential negative effects could be mitigated and it could have a beneficial impact on EU energy security by bringing new gas to market.

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